

SUBJECT: Public school finance revisions

COMMITTEE: Public Education: committee substitute recommended

VOTE: 8 ayes — Glossbrenner, Luna, Colbert, Arnold, Berlanga, Fraser, Grusendorf, Schoolcraft

1 nay — Blair

SENATE VOTE: On final passage, Feb. 20: 20-7 (Bivins, Brown, C. Harris, O.H. Harris, Krier, Leedom, Sims)

WITNESSES: None

BACKGROUND: **Edgewood I.** On Oct. 2, 1989 the Texas Supreme Court, ruling in *Edgewood ISD v. Kirby* ("Edgewood I"), found the Texas school-finance system unconstitutional. After four special sessions on school finance, from Feb. 28 to June 6, 1990, SB 1 by Parker, 71st Legislature, sixth special session, was enacted. The bill revised the public-education finance system, changed the structure of state education administration, added several education-accountability measures and made other changes governing public schools. (For a detailed explanation of the provisions of SB 1, see House Research Organization Special Legislative Report No. 160, *Wrap-up of the 1990 Special Sessions on Public Education*, July 31, 1990.)

The finance system in SB 1 was reviewed by Dist. Judge F. Scott McCown, who in September ruled it unconstitutional because "it continues to deny school districts 'substantially equal access to similar revenues per pupil at similar levels of tax effort.'" The non-finance provisions of SB 1 were not challenged in court.

Edgewood II. Judge McCown's opinion was appealed directly to the Texas Supreme Court, which on Jan. 22, 1991 issued a unanimous opinion ("Edgewood II"), written by Chief Justice Tom Phillips, that declared the school-finance system enacted by SB 1 unconstitutional. The Supreme Court gave the Legislature until April 1, 1991 to enact a constitutional system, to be in place by Sept. 1, 1991, or face an

injunction against distributing any money under the school-finance system.

The Supreme Court ruled that "to be efficient, a funding system that is so dependent on local ad valorem property taxes must draw revenue from all property at a substantially similar rate."

The court said "we do not prescribe the means which the Legislature must employ in fulfilling its duty," but did add that "consolidation of school districts is one available avenue toward greater efficiency in our school finance system" and "another approach to efficiency is tax base consolidation."

On Feb 14, 10 House members (Reps. Fred Blair, Wilhelmina Delco, Kent Grusendorf, Allen Hightower, Libby Linebarger, Parker McCollough, Nicolas Perez, Jim Rudd, Mark Stiles and Ric Williamson), represented by Rep. Robert Junell, filed a motion for rehearing with the Supreme Court. The motion asked the court to consider certain questions the members "find critical to enactment of legislation that meets the standards announced by the court."

Feb. 25 opinion. On Feb. 25 the Supreme Court issued an opinion on the House members' motion, written by Chief Justice Tom Phillips (author of "Edgewood II") and joined by four other justices. A dissent was issued by Justices Lloyd Doggett and Oscar Mauzy (author of "Edgewood I"), joined by Justice Bob Gammage, and a separate dissent was issued by Justice Raul Gonzalez.

The majority opinion declined to overrule or modify the court's 1931 ruling in *Love v. City of Dallas*, 40 S.W.2d 20, that prohibits the state from requiring a school district to give local tax revenue up for education of students who do not reside in the district. The majority stated that "tax base consolidation could be achieved through the creation of new school districts . . . These school districts could be organized along county or other lines and could be given the authority to generate local property tax revenue for all of the other school districts within their boundaries." However, "local tax revenue is not subject to state-wide recapture," according to the majority.

The majority opinion also addressed the question of "whether the Legislative may constitutionally authorize school districts to generate and spend local taxes to enrich or supplement an efficient system" and concluded that "the Constitution does permit such enrichment, without equalization."

The opinion stated that "the current system remains unconstitutional not because *any* unequalized local supplementation is employed, but because the state relies so heavily on unequalized local funding in attempting to discharge its duty" to maintain an efficient system of public schools. Therefore, "once the Legislature provides an efficient system in compliance with [the Constitution], it may, so long as efficiency is maintained, authorize local school districts to supplement their educational resources if local property owners approve an additional property tax."

The court reaffirmed, "Our deadline of April 1, 1991, for legislative action remains unchanged."

The dissent written by Justice Doggett focused on the advisability of issuing an opinion, rather than on the content of the opinion. Doggett stated that the majority opinion "constitutes a frantic rush to influence the final stages of current legislative deliberations and will only prolong correction of our inefficient educational system at the expense of the school children of Texas." The dissent added, "Our decision on local enrichment in *Edgewood I* was straightforward and has been a puzzle primarily to those who preferred not to comprehend it or who disliked what they read. As a postscript to the court's prior unanimous writings, this most recent effort adds more confusion than clarity."

System basics. The Texas school system has about 1,060 independent school districts operating in 254 counties. Each district may levy a tax of up to a constitutionally imposed cap of \$1.50 per \$100 in property valuation for local school maintenance and operations (the M&O tax rate) and a separate tax to finance school facilities or bond debt (the debt-service tax or bond tax). The state provides additional funding through a two-tier funding mechanism called the Foundation School Program. The Texas Education Agency reports that in the 1989-90

school year, the last year for which figures are available, the average effective M&O tax rate was 81.3 cents and the average effective debt-service tax was 14.7 cents, for a total rate of 96 cents. (Effective tax rates are adjusted to facilitate statewide comparisons and differ somewhat from "nominal," or stated tax rates.)

Senate Bill 1 (1990)

The Foundation School Program — first tier

The bulk of state support for public education is currently provided through the two tiers of the Foundation School Program (FSP). The amount of FSP aid a district gets from the state depends on the district's wealth, tax rate, size and type of students. Local districts levy taxes to raise a share of the FSP and may raise additional revenues to enrich their programs and to retire bonds issued to finance school facilities.

Basic allotment. The first tier of FSP funding is intended to guarantee each district enough money to provide a basic education program. The amount distributed to each school district is determined by statutory formulas that start with a basic per-pupil allotment, set by SB 1 at \$1,910 for 1990-91 and \$2,128 in subsequent years.

The basic allotment is adjusted by a "cost-of-education index" (CEI) adopted biennially by the Foundation School Fund Budget Committee (governor, lieutenant governor and comptroller) that adjusts for regional price variations and district attendance. The basic allotment, adjusted by the CEI is multiplied by a district's average daily attendance to determine a basic per-student entitlement. The state share of the basic entitlement is distributed to school districts as a block grant for operating costs.

Weighted pupil allotments. Districts receive extra money for students in vocational education, special education, programs for the gifted and talented and for compensatory and bilingual education. The distributions are determined by multiplying the number of students in each special program by a "weight" assigned to each program.

Local share. The basic ("first tier") FSP cost equals the sum of the basic entitlement block grant, the special-program allotment based on student weights, career ladder allotments ("merit" teacher-salary supplements), and transportation allotments. Local districts pay a portion of this amount, called the local share. Under SB 1, the local share is the amount raised by a tax rate of 54 cents per \$100 of property value in 1990-91 and 70 cents thereafter.

Second tier of the FSP — the Guaranteed Yield Program

The state offers a second tier of aid under the Foundation School Program: equalization funding distributed through the Guaranteed Yield Program to help property-poor districts enrich programs. The program guarantees each district a specified amount per weighted student in state and local funds, for each cent of tax effort over that required for the local fund assignment, up to a specified maximum level.

SB 1 set the guaranteed state-local yield for each cent of tax rate above the rate required for a district's local fund assignment at \$17.90 per weighted student for the 1990-91 school year and \$26.05 per weighted student in subsequent years. The tax rate above the mandatory local-fund-assignment tax rate for which the yield is guaranteed by the state was set by SB 1 at 37 cents per \$100 for 1990-91 and 48 cents thereafter. Tax effort greater than 91 cents per \$100 in 1990-91 (54-cent first-tier tax rate plus 37-cent guaranteed-yield rate) or \$1.18 (70-cent first tier rate plus 48-cent guaranteed-yield rate) is not matched by the state. Money received under the Guaranteed Yield Program, unlike first-tier FSP allocations, may be used for capital outlays and debt service.

Proration of state aid

HB 72 (1984) established a "sum certain" ceiling on state costs under the Foundation School Program. If the total state share of the FSP, as determined by the formulas governing the program, is greater than the total amount appropriated by the Legislature to the FSP for that year, each district's allocation of state funds must be reduced according to a formula adopted by the State Board of Education.

The current formula requires a proportionately smaller reduction in allocations to districts with low wealth and high tax effort and a proportionately greater reduction for districts with high wealth and low tax effort. (Tax effort, or effective tax rate, reflects actual tax collections per \$100 of taxable property value. The effective tax rate is used in place of the listed tax rate to take into account delinquent taxes and variations in assessment ratios.) Of districts with equal property value, the district with the greater tax effort would bear a lower prorated reduction in state aid per student. Of districts with equal tax effort, the district with the lower taxable property value per student would bear the lower prorated reduction per student.

DIGEST:

CSSB 351 would revise the public-education finance system, starting in the 1991-92 school year, creating a four-level funding system utilizing 195 county education districts. School districts within a county district would share revenue from a 60-cent minimum M&O tax that would have to be levied for the next school year by all school districts.

The bill also would reenact some finance provisions (Chapter 16 of the Education Code), that were invalidated by the Texas Supreme Court in the Edgewood II decision. The bill would not modify the non-finance changes made by SB 1, including changes in the structure of state education administration and new education-accountability measures. Most provisions of the bill would take effect Sept. 1, 1991.

CSSB 351 would make no appropriation. The Legislative Budget Office estimates that the bill's funding formulas would cost the state an additional \$1.03 billion in fiscal 1992-93, at current 1991 local tax rates, or an additional \$837.6 million in 1992-93, if all districts raised their tax rates to the maximum rate for which the state would guarantee state aid. In addition, the state's contribution to the Teacher Retirement System would increase by \$54.6 million in 1992-93. These costs are in comparison to the amount appropriated for 1991 (SB 11, 71st Legislature, sixth special session), rather than to the projected state costs for 1992-93 under SB 1, since the finance provisions of SB 1 are unenforceable after Sept. 1, 1991.

Basic structure

CSSB 351 would create a Foundation School Program of three funding tiers and a separate facilities component. The first tier would guarantee funding for a basic program meeting accreditation and other legal standards; the second tier would provide guaranteed-yield funding for program enrichment and facilities; the third tier would consist of a pooled fund within each county education district for additional revenue. The facilities component would be a separate, guaranteed-yield program for capital outlay and debt service, starting in the 1992-93 school year.

County education districts. CSSB 351 would create 189 county education districts. Each district would consist of a single county or a group of counties, selected so that no district had a taxable property value greater than \$260,000 per weighted student, or a higher ceiling set by the Foundation School Fund Budget Committee (FSFBC).

The bill would take ("recapture") some revenue raised by certain wealthier school districts through local taxes designated for each tier or component and redistribute them to lower-wealth school districts within the same county education district. The governing board of a school district included in a county education district would retain its authority to manage the public schools in the district and to levy, assess and collect property taxes.

First tier

Basic allotment. The basic per-student allotment, used to calculate the first funding tier in the Foundation School Program, would be decreased from the \$2,128 currently scheduled by current law (SB 1) for the 1991-92 school year to \$2,020 for 1990-91. The basic allotment would be increased to \$2,130 for the 1992-93 school year, \$2,270 for 1993-94 and \$2,400 for 1994-95 and thereafter or, beginning with the 1993-94 school year, an amount adopted by the Foundation School Fund Budget Committee (FSFBC).

The bill would retain SB 1's provision to set, starting in 1993-94, the basic allotment to represent the cost per student of a regular education

program meeting the basic criteria for an accredited program meeting all legal and regulatory mandates and to use the cost-of-education index designed to reflect the geographic variation in costs that are beyond the control of school districts.

Local share. The computation of the local-district share of the foundation program would be changed. (The local share was set by SB 1, at the amount raised by a tax rate of 54 cents per \$100 of property value for the 1991-92 school year, and thereafter at the amount raised by an effective tax rate of 70 cents or, in 1993-94 and 1994-95, a rate adopted by the FSFBC.) The new local share would be the amount raised by an effective tax rate of 60 cents in 1991-92, 70 cents in 1992-93, 75 cents in 1993-94 and 80 cents in subsequent years. The FSFBC could set a different tax rate for 1993-94 and thereafter.

The commissioner of education would be required to order the immediate suspension of the powers of a school district that failed to set a tax rate at least equal to the local-share rate. The commissioner would appoint a district superintendent to reset the rate.

Recapture. If the amount raised by a school district at its local share tax rate, plus the per-capita distribution to the district from the Available School Fund, exceeded the cost of the first-tier program in that district, the district would have to remit the excess to an entity designated by the comptroller to receive the funds. The funds would be redistributed to other school districts within the same county education district that are unable to generate the full amount at their first-tier entitlement at their local-share tax rate.

Second tier (guaranteed yield program)

Guaranteed yield. The guaranteed state-local revenue yield to each district for each cent of tax rate above the rate the district levies for its local share of the foundation program would be changed. (The guaranteed yield is now \$17.90 per weighted student for the 1990-91 school year and \$26.05 thereafter established by SB 1.) The guaranteed yield would be \$20 for the 1991-92 school year, \$22 for 1992-93, \$24 for 1993-94 and \$26 for 1994-95 and thereafter. Starting in 1993-94,

the FSFBC could adopt a different amount, as permitted by SB 1. (The weights applied to second-tier, third-tier and facilities funding calculations would include full program weights, one-half the cost-of-education index adjustment, and no career ladder or transportation allotments, as under SB 1.)

District enrichment tax rate. The maximum district enrichment tax rate — the maximum tax rate, above the mandatory local-share tax rate, for which the yield is guaranteed by the state — would be changed. (The rate is now 37 cents per \$100 of property valuation for the 1990-91 school year and 48 cents thereafter.) The rate would be 40 cents for 1991-92, 45 cents for 1992-93, 30 cents for 1993-94 and thereafter. As under SB 1, the FSFBC could set a different rate starting in 1993-94.

In 1991-92 and 1992-93, the tax rate eligible for the state-guaranteed yield could, at a district's option, combine the district's maintenance-and-operation (M&O) tax rate and its bond-debt tax rate. Thereafter, only the M&O rate could be considered in the second tier.

Recapture. If the amount per weighted student generated by a school district for each penny of tax rate (its "yield per penny") exceeded the amount per weighted student per penny guaranteed by the state, the district would have to remit the excess tax revenue generated by the second-tier tax rate to an entity designated by the comptroller to receive the funds. The excess funds would be redistributed to lower-yield school districts within the same county education district (those with a yield lower than the state-guaranteed yield.)

Facilities component

The facilities-funding component would provide districts a guaranteed-yield tax program that could be used exclusively for capital outlay or debt service. The facilities funding component, which would start with the 1993-94 school year, would be structured exactly like the second-tier guaranteed-yield program.

Guaranteed yield. The guaranteed state-local revenue yield for each cent of tax rate over the mandatory local-share rate would be \$24 per

weighted student for the 1990-91 school year and \$26 thereafter or a rate adopted by the FSFBC.

District facilities tax rate. The district facilities tax rate — the bond-tax rate for which the revenue yield would be guaranteed by the state — would be 20 cents per \$100 of property valuation for the 1993-94 school year and thereafter or a different rate adopted by the FSFBC.

Recapture. If the amount per weighted student generated by a school district for each penny of its bond-tax rate (its "yield per penny") exceeded the amount per weighted student per penny guaranteed by the state, the excess funds would be redistributed to lower-yield school districts within the same county education district (those with a yield lower than the state-guaranteed yield).

If the amount generated by a district through the facilities component fell below the district's debt-service requirements for debt incurred before April 1, 1991, the district could levy and retain a bond tax greater than the maximum rate eligible for the state-guaranteed yield. Any bond-tax collections exceeding debt-service requirements would be redistributed within the county education district.

Standards. All facilities constructed by school districts after Sept. 1, 1992 would be required to meet standards established by the State Board of Education for adequacy of school facilities in order to be financed with state or local tax funds.

Third tier

A third funding tier would pool local-district tax revenue within a county education district for redistribution within that county district. Any maintenance tax collections generated by a district's tax effort above the level required for tier one and necessary for the district to maximize state aid in tier two and the facilities component would be redistributed within the same county education district. Districts would receive the revenue in proportion to their third-tier tax effort per weighted student, subject to certain phase-in requirements.

Phase-in. The third-tier distribution would be phased in so that each district participating in third-tier funding would receive back a portion of the amount by which its 1990-91 spending per weighted student exceeded the 1994-95 guaranteed tier one and tier two revenue. In school year 1991-92 each district would receive back, before any distribution within the county district, up to 75 percent of the third-tier collections it had remitted; in 1992-93, up to 50 percent, and in 1993-94, up to 25 percent.

Accountable cost studies. The biennial studies of accountable costs conducted by the Legislative Education Board (LEB) and Legislative Budget Board (LBB), with the assistance of the Educational Economic Policy Center and the Texas Education Agency, (designed to provide a research basis for the adoption by the FSFBC of the funding elements necessary to meet the state policy goals of the school-finance system) would not be prohibited from including the costs of cocurricular and extracurricular programs or required to include only costs necessary for operation, maintenance and administration and costs necessary for adequate facilities and equipment. The biennial studies would include a study of the impact of the levels of pooled enrichment funds under the third tier (county education district distributions). No study of the accountable costs per student of exemplary programs would be done.

Severability

If any provision of CSSB 251 or its application to any person or circumstance were held to be invalid by a court, the remaining provisions or applications that could be given effect without the invalid provision or application would become effective.

NOTES:

Limit on debate

The Calendars Committee has adopted a rule limiting amendments to SB 351, using its authority under House Rule 3, sec. 4 (2). The rule will limit amendments to those dealing with allocation of state and local funds for financing public schools. The rule is to be strictly interpreted to limit debate.

Comparison of CSSB 351 with Senate version of SB 351

Basic structure. The basic structure of SB 351, as passed by the Senate, differs from the House committee substitute for the bill in only a few significant respects. Both versions would create a Foundation School Program consisting of four funding components (in Senate version, four tiers; in the House committee substitute, three tiers and a separate facilities component).

The Senate version would redistribute funds within 20 regional education districts established by the State Board of Education (SBOE); the House committee substitute would use 195 county education districts created by the Legislature. The regional districts would each include at least 50,000 students, have boundaries that did not cross school-district lines, contain a regional education service center, have the same boundaries as that center's service center, and have the highest possible degree of similarity in property wealth per student with other regional districts. A school district would be able to petition the SBOE for transfer from one regional district to another. The board could grant any with an educational benefit, if it would not increase the disparity in property wealth per student between the districts involved.

The Senate version specifies that if the Texas Constitution were amended to permit the Legislature to redistribute taxes collected by one school district among other school districts, the provisions of the Senate version concerning regional education districts would not take effect and redistribution would take place statewide.

First tier. The first tier of the Senate version would provide a higher basic allotment than the House substitute: \$2,170 for the 1991-92 school year in the Senate version, \$2,020 in the House substitute; \$2,325 for 1992-93 in the Senate version, \$2,130 in the House substitute; \$2,525 for 1993-94 in the Senate version, \$2,270 in the House substitute; and \$2,760 for 1994-95 in the Senate version, \$2,400 in the House substitute. The local-share tax rate would be higher in the Senate version: 70 cents per \$100 of property value for the 1991-92 school year in the Senate version, 60 cents in the House substitute; 80 cents for 1992-93 in the Senate version, 70 cents in the House

substitute; 90 cents for 1993-94 in the Senate version, 75 cents in the House substitute; \$1.00 for 1994-95 and thereafter in the Senate version, 80 cents in the House substitute.

The first-tier recapture provision of the Senate version is similar to those of the House substitute. The Senate version would reallocate excess funds from a school district within the district's regional education district under rules prescribed by the State Board of Education; the House substitute would reallocate within the district's county education district according to a statutory formula.

The Senate version would distribute the Technology Fund allotments (established by SB 1, effective Sept. 1, 1992) through the Foundation School Program.

Enrichment tier. The enrichment tier (based on the current guaranteed-yield program of SB 1) is referred to as "tier 3" in the Senate version, but as "tier 2" in the House substitute. The enrichment-tier guaranteed state-local yield would be the same in both the Senate version and the House substitute — \$20 for the 1991-92 school year, \$22 for 1992-93, \$24 for 1993-94 and \$26 for 1994-95 and thereafter. The maximum district enrichment tax rate (the tax rate for which the yield would be guaranteed by the state in the enrichment tier) would be the same in both the Senate version and the House substitute — 40 cents per \$100 of property valuation for the 1991-92 school year, 45 cents for 1992-93, and 30 cents for 1993-94 and thereafter.

In the Senate version the district enrichment tax rate would be the *total* local tax rate above the sum of the mandatory local-share tax rate and the facilities-tier tax rate; the House committee substitute would apply to the maintenance and operation tax rate only. However, the House substitute would allow a district to include its bond-tax rate in calculating the enrichment-tier program in 1991-92 and 1992-93.

The enrichment-tier recapture provisions differ in the same way as the first-tier recapture provisions.

Facilities. The facilities provisions of the Senate version are identical to those of the House committee substitute in the amount of yield guaranteed per penny per weighted student and the tax rate eligible for the program. The facilities recapture provisions differ in the same way as the first tier and the enrichment tier.

The Senate version treats the facilities program as a second tier — the guaranteed-yield enrichment-tier tax rate is reached only after the debt-service and facilities tier tax rate has been subtracted. The House substitute treats the facilities program as a separate component that does not affect the tax rate used to calculate the enrichment tier. (The House substitute would allow a district to include its bond-tax rate in calculating the enrichment-tier program in 1991-92 and 1992-93.)

Supplemental tier

The Senate version would offer a fourth tier, consisting of a guaranteed yield program without recapture, intended to give each district an opportunity to supplement the program level provided by the first and third tiers of the Senate version.

For each penny of maintenance-and-operation tax effort over the mandatory local-share tax rate, plus the maximum district enrichment rate (for the guaranteed-yield enrichment program), the Senate version would guarantee a state-local yield per weighted student equal to the yield per weighted student of the district at the 97th percentile of property wealth per weighted student. (The 97th-percentile district is the one at the point at which 97 percent of the weighted students in the state are in districts with state and local revenue per weighted student equal to or less than that of the 97th-percentile district.)

The maximum tax rate eligible for the state-guaranteed yield under this tier would be the rate that, at the state-guaranteed yield, would generate the level of revenue equal to 10 percent of the statewide total state and local revenue per weighted student for the foundation and enrichment tiers (in the Senate version, the first and third tiers). Districts above the 97th percentile of property wealth per student would be limited to the rate that, applied to their own property wealth per weighted student,

would generate the level of revenue equal to 10 percent of the statewide total state and local revenue per weighted student for the foundation and enrichment tiers.

A district's effective tax rate would be capped at \$1.50 under the Senate version, unless necessary to pay principal and interest on debt previously incurred by the district.

Phase-in of recapture. The Senate version would phase in the recapture provisions, which affect the first three tiers (local share, enrichment and facilities), over four years. In the 1991-92 school year, a district would remit to its regional education district 25 percent of the excess tax revenue that would otherwise be recaptured. In 1992-93 a district would remit 50 percent of the amount that would otherwise be recaptured; in 1993-94 it would remit 75 percent. The House substitute would not phase-in recapture but would provide phased refunds to districts of additional spending per student before their tax revenue was pooled and redistributed under tier 3.

Proration. The Senate version would require that, if appropriations were not sufficient to cover the full state share of the Foundation School Program as determined by formula, the state funds allocated under the fourth (supplemental) tier would be reduced by the shortfall, up to one-half of the state's share of the tier. Any additional shortfall would be prorated across the other three tiers.

Available School Fund. The Senate version would require the Available School Fund to be distributed monthly to the Foundation School Fund, rather than apportioned annually to each school district on a per-capita basis. The House substitute would include a district's Available School Fund distribution in determining how much, if any, excess revenue it had to remit to the county educational district.

State policy. The Senate version would commit the public school finance system to a standard of neutrality that *guaranteed* substantially equal access to *equal* revenue per student for *all* students at *any* tax rate, rather than a standard of fiscal neutrality that *provided for*

substantially equal access to *similar* revenue per student for *similar* tax effort.

Tax collection rules. The Senate version would permit the comptroller to adopt rules for the administration, collection and redistribution of the property taxes subject to the four tiers and to review the efficiency of a school district's tax collection effort.